

As a general rule, such transportation property will be considered to be used predominantly outside the United States if 70 percent or more of the miles traversed (during the taxable year at the close of which a determination is made under section 956(a)(2)) in the use of such property are traversed outside the United States or if such property is located outside the United States 70 percent of the time during such taxable year. Notwithstanding the above, an aircraft or vessel (as the term is defined in § 1.954-2T(c)(2)(ii)) is excluded from U.S. property if rents derived from leasing such aircraft or vessel are excluded from foreign personal holding company income under section 954(c)(2)(A). See paragraph (e) of this section for the effective/applicability dates of this paragraph (b)(1)(vi).

(c) through (d)(1) [Reserved] For further guidance, see § 1.956-2(b)(1)(vii) through (d)(1).

(2) *Obligation defined*—(i) *Rule*. For purposes of § 1.956-2 of the regulations, the term “obligation” includes any bond, note, debenture, certificate, bill receivable, account receivable, note receivable, open account, or other indebtedness, whether or not issued at a discount and whether or not bearing interest, except that such term shall not include:

(A) Any indebtedness arising out of the involuntary conversion of property which is not United States property within the meaning of paragraph (a)(1) of § 1.956-2, or

(B) Any obligation of a United States person (as defined in section 957(c)) arising in connection with the provision of services by a controlled foreign corporation to the United States person if the amount of such obligation outstanding at any time during the taxable year of the controlled foreign corporation does not exceed an amount which would be ordinary and necessary to carry on the trade or business of the controlled foreign corporation and the United States person if they were unrelated. The amount of such obligations shall be considered to be ordinary and necessary to the extent of such receivables that are paid within 60 days.

See § 1.956-2(b)(1)(v) for the exclusion from United States property of obligations arising in connection with the

sale or processing of property where such obligations are ordinary and necessary as to amount.

(ii) *Effective date*. This section is effective June 14, 1988, with respect to investments made on or after June 14, 1988.

(e) *Effective/applicability date*. Paragraph (b)(1)(vi) of this section applies to taxable years of controlled foreign corporations beginning on or after May 2, 2006, and for tax years of United States shareholders with or within which such tax years of the controlled foreign corporations end. Taxpayers may elect to apply the rule of this section to taxable years of controlled foreign corporations beginning after December 31, 2004, and for tax years of United States shareholders with or within which such tax years of foreign corporations end. If an election is made to apply § 1.954-2T(c) to taxable years of a controlled foreign corporation beginning after December 31, 2004, then the election must also be made for paragraph (b)(1)(vi) of this section.

(2) *Expiration date*. The applicability of paragraph (b)(1)(vi) of this section will expire on July 1, 2011.

[T.D. 8209, 53 FR 22171, June 14, 1988, as amended at T.D. 9406, 73 FR 38117, July 3, 2008]

**§ 1.956-3T Certain trade or service receivables acquired from United States persons (temporary).**

(a) *In general*. For purposes of section 956(a) and § 1.956-1, the term “United States property” also includes any trade or service receivable if the trade or service receivable is acquired (directly or indirectly) after March 1, 1984, from a related person who is a United States person (as defined in section 7701(a)(30)) (hereinafter referred to as a “related United States person”) and the obligor under the receivable is a United States person. A trade or service receivable described in this paragraph shall be considered to be United States property notwithstanding the exceptions (other than subparagraph (H)) contained in section 956(b)(2). The terms “trade or service receivable” and “related person” have the respective meanings given to such terms by section 864(d) and the regulations thereunder. For purposes of this

section, the exception contained in § 1.956-2T(d)(2)(i)(B) for short-term obligations shall not apply to service receivables described in this paragraph.

(b) *Acquisition of a trade or service receivable*—(1) *General rule.* The rules of § 1.864-8T(c)(1) shall be applied to determine whether a controlled foreign corporation has acquired a trade or service receivable.

(2) *Indirect acquisitions*—(i) *Acquisition through unrelated person.* A trade or service receivable will be considered to be acquired from a related person if it is acquired from an unrelated person who acquired (directly or indirectly) such receivable from a person who is a related person to the acquiring person.

(ii) *Acquisition by nominee or pass-through entity.* A controlled foreign corporation will be considered to have acquired a trade or service receivable of a related United States person held on its behalf:

(A) By a nominee or by a partnership, simple trust, S corporation or other pass-through entity to the extent the controlled foreign corporation owns (directly or indirectly) a beneficial interest in such partnership or other pass-through entity; or

(B) By another foreign corporation that is controlled by the controlled foreign corporation, if one of the principal purposes for creating, organizing, or funding such other foreign corporation (through capital contributions or debt) is to avoid the application of section 956. See § 1.956-1T.

The rule of this paragraph (b)(2)(ii) does not limit the application of paragraph (b)(2)(iii) of this section regarding the characterization of trade or service receivables of unrelated persons acquired pursuant to certain swap or pooling arrangements. The following examples illustrate the application of this paragraph (b)(2)(ii).

*Example 1.* FS1, a controlled foreign corporation with substantial accumulated earnings and profits, contributes \$2,000,000 to PS, a partnership, in exchange for a 20 percent limited partnership interest in PS. PS purchases trade or service receivables of FS1's domestic parent, P. The obligors under the receivables are United States persons. PS does not purchase receivables of any person who is related to any other partner in PS. Under paragraph (b)(2)(ii)(A) of this section, there is an investment of the earnings of FS1

in United States property equal to 20 percent of PS's basis in the receivables of P.

*Example 2.* FS1, a controlled foreign corporation, has accumulated more than \$3,000,000 in earnings and profits. It organizes a wholly-owned foreign corporation, FS2, with a \$2,000,000 equity contribution. FS2 has no earnings and profits. FS2 uses the funds to purchase trade or service receivables of FS1's domestic parent, P. The obligors under the receivables are United States persons. Under paragraph (b)(2)(ii)(B) of this section, there is an investment of the earnings of FS1 in United States property equal to \$2,000,000.

(iii) *Swap or pooling arrangements.* A trade or service receivable of an unrelated person will be considered to be a trade or service receivable acquired from a related United States person and subject to the rules of this section if it is acquired in accordance with an arrangement that involves two or more groups of related persons that are unrelated to each other and the effect of the arrangement is that one or more related persons in each group acquire (directly or indirectly) trade or service receivables of one or more unrelated United States persons who are also parties to the arrangement, in exchange for reciprocal purchases of receivables of United States persons in the first group. The following example illustrates the application of this paragraph (b)(2)(iii).

*Example.* Controlled foreign corporations A, B, C, and D are wholly-owned subsidiaries of domestic corporations M, N, O, and P, respectively. M, N, O, and P are not related persons. According to a prearranged plan, A, B, C, and D each acquire trade or service receivables of M, N, O, and/or P. The obligors under some or all of the receivables acquired by each of A, B, C, and D are United States persons. Because the effect of this arrangement is that the unrelated groups acquire each other's trade or service receivables of United States persons pursuant to the arrangement, there is an investment of the earnings of each of A, B, C, and D in United States property to the extent of the purchase price of those receivables under which the obligors are United States persons.

(iv) *Financing arrangements.* If a controlled foreign corporation participates (directly or indirectly) in a lending transaction that results in a loan to a United States person who purchases property described in section 1221(1) (hereinafter referred to as "inventory property") or services of a related

United States person, or to any person who purchases trade or service receivables of a related United States person under which the obligor is a United States person, or to a person who is related to any such purchaser, and if the loan would not have been made or maintained on the same terms but for the corresponding purchase, then the controlled foreign corporation shall be considered to have indirectly acquired a trade or service receivable described in paragraph (a) of this section. For purposes of this paragraph (b)(2)(iv), it is immaterial that the sums lent are not, in fact, the sums used to finance the purchase of the inventory property or services or trade or service receivables of a related United States person. The amount to be taken into account with respect to the controlled foreign corporation's investment in United States property (resulting from application of this paragraph (b)(2)(iv)) shall be the amount lent pursuant to a lending transaction described in this paragraph (b)(2)(iv), if the amount lent is equal to or less than the purchase price of the inventory property, services, or trade or service receivables. If the amount lent is greater than the purchase price of the inventory property, services or receivables, the amount to be taken into account shall be the purchase price. The following examples illustrate the application of this paragraph (b)(2)(iv).

*Example 1.* P, a domestic corporation, owns all of the outstanding stock of FS1, a controlled foreign corporation. P sells equipment for \$2,000,000 to X, an unrelated United States person. FS1 makes a \$1,000,000 short-term loan to X, which loan would not have been made or maintained on the same terms but for X's purchase of P's equipment. Because FS1 directly participates in a lending transaction described in this paragraph (b)(2)(iv), FS1 is considered to have acquired the receivable of a related United States person. Thus, there is an investment of FS1's earnings and profits in United States property in the amount of \$1,000,000.

*Example 2.* The facts are the same as in Example 1, except that instead of loaning money to X directly, FS1 deposits \$3,000,000 with an unrelated financial institution that loans \$2,000,000 to X in order for X to purchase P's equipment. The loan would not have been made or maintained on the same terms but for the corresponding deposit. Accordingly, the deposit and the loan are treat-

ed as a direct loan from FS1 to X. *See* Rev. Rul. 87-89, 1987-37 I.R.B. 16. Because FS1 indirectly participates in a lending transaction described in this paragraph (b)(2)(iv), FS1 is considered to have acquired the receivable of a related United States person. Thus, there is an investment of FS1's earnings and profits in United States property in the amount of \$2,000,000.

*Example 3.* P, a domestic corporation, owns all of the outstanding stock of FS1, a controlled foreign corporation. FS1 makes a \$3,000,000 loan to U, an unrelated foreign corporation, in connection with U's purchase for \$2,000,000 of receivables from the sale of inventory property by P to United States obligors. Because FS1 directly participates in a lending transaction described in this paragraph (b)(2)(iv), FS1 is considered to have acquired receivables of a related United States person. Thus, there is an investment of FS1's earnings and profits in United States property in the amount of \$2,000,000.

(c) *Substitution of obligor.* For purposes of this section, the substitution of another person for a United States obligor may be disregarded. Thus, if a purchaser who is a United States person arranges for a foreign person to pay a United States seller of inventory property or services and the seller transfers by sale or otherwise to its own controlled foreign corporation the foreign person's obligation for payment, then the acquisition of the foreign person's obligation shall constitute an investment in United States property by the seller's controlled foreign corporation, unless it can be demonstrated by the parties to the transaction that the primary purpose for the arrangement was not the avoidance of section 956. The following example illustrates the application of this paragraph.

*Example.* P, a domestic corporation, owns all of the outstanding stock of FS1, a controlled foreign corporation with substantial accumulated earnings and profits. P sells equipment to X, a domestic corporation unrelated to P. To pay for the equipment, X arranges for a foreign financing entity to issue a note to P. P then sells the note to FS1. FS1 has made an investment in United States property in the amount of the purchase price of the note.

[T.D. 8209, 53 FR 22169, June 14, 1988]